

Government continues to be confused about Software Industry – July 11, 2009

Government continues to be confused about Software Industry : By S Sivakumar, CA

That the Government continues to be confused about the Software Sector needs no further proof. One has only to look into the Budget Speech of Mr Pranob Mukherjee and the text of Notification No. 22/2009-ST dated July 7, 2009 and the Explanatory Notes and the customary Joint Secretary's letters.

While announcing the Budget in the Parliament earlier today, this is what the FM had to say, in Para 124 of his Budget speech.

Quote :

124. The IT industry has pointed out that it is facing difficulties in the assessment of software which involves transfer of the right to use after the levy of service tax on IT software service. To resolve the matter, I propose to exempt the value attributable to the transfer of the right to use packaged software from excise duty and CVD.

Unquote :

As per Notification No. 22/2009-ST dated July 7, 2009, packaged software or canned software, falling under Chapter 85 of the First Schedule to the Central Excise Tariff Act, 1985 is exempted to the extent of the value representing the consideration paid or payable for transfer of the right to use such goods provided that the transfer of the right to use shall be for commercial exploitation including the right to reproduce, distribute and sell such software and the right to use the software components for the creation of and inclusion in other information technology software products and also provided further that the person providing the right to use shall make a declaration to this effect to the Assistant Commissioner of Central Excise or the Deputy Commissioner of Central Excise, as the case may be, in respect of such transfer of the right to use for commercial exploitation provided also that the person providing the right to use shall be registered with the Service Tax Department under Section 69 of the Finance Act, 1994.

It is clear that the Government wants to exempt the value of the software licenses from the value of packaged software sold by software manufacturers for purposes of levy of central excise duty.

I am quite confused about this new googly from the Government and have shared my reactions, as under. Firstly, most, if not all, of the packaged software is covered by the licensing route. Most software product companies give or transfer licenses to the users of their packaged software. I have not come across any instance by which a packaged software manufacturer sells software for a value, a portion of which is attributable to the right to use the software. The commonest method used by the packaged software industry is to license their software products for a fee and consequently, the value of the packaged /canned software would be equivalent to the value of the software license given. It would then mean that, packaged software licensed out would not suffer any central excise duty.

Secondly... I am not able to understand if software licenses were ever subjected to the levy of central excise duty in the first place, irrespective of whether the licenses were transferred electronically or not, despite the central excise tariff under Chapter 85. I am not aware of a software product company paying central excise duty, by the way. I only hope that this Notification does not result in the Central Excise Department asking packaged software developers to pay excise duty for the past years, which could have disastrous implications.

Thirdly...as per Section 65(105)(zzzze)(vi) of the Finance Act, 1994, acquiring ('providing' as a result of the amendment) the right to use information technology software supplied electronically is a taxable service. Many of have pointed out that, licensing out software products/package software results in a double taxation, in as much as, the same transaction gets taxed as sale of goods under the State VAT laws and as services under the Finance Act, 1994. This situation would continue, unfortunately, as the Budget has made no attempt to remove the double taxation belying expectations of the IT sector.

Fourthly... what would happen, in cases, where the so called manufacturer of packaged software is different from the distributor of the packaged software? I would look up to the Heavens for an answer.

Before concluding...

Has the Budget changed the levy of indirect taxes for the Software Industry? No and absolutely no, Sir. Software licenses, whether related to packaged software or customized software, would continue to suffer both VAT and Service Tax, despite all expectations to the contrary.

On the other hand, ironically, packaged software 'manufacturers' should now look forward to some trouble from the Central Excise Department, in terms of levy of central excise duty.

Quote of the Day: The easiest thing to find is fault. –Anonymous